DOCUMENT RESUME

ED 293 395 HE 021 147

TITLE	Invitational Conference on College Prepayment and Savings Plans (Denver, Colorado, June 7-8, 1987). Summary.
INSTITUTION	College Entrance Examination Board, New York, N.Y.
SPONS AGENCY	American Council on Education, Washington, D.C.; Education Commission of the States, Denver, Colo.; National Center for Postsecondary Governance and Finance, College Park, MD.
PUB DATE	Jul 87
NOTE	31p.
AVAILABLE FROM	College Board Publications, Box 886, New York, NY 10101-0886 ($10.00 for the conference summary and full proceedings).
PUB TYPE	Collected Works - Conference Proceedings (021)
EDRS PRICE	MF01 Plus Postage. PC Not Available from EDRS.
DESCRIPTORS	Access to Education; College Students; Educational Equity (Finance); Educational Finance; Financial Policy; Financial Support; Higher Education; Insurance; Investment; *Parent Financial Contribution; State Legislation; State Programs; Student Costs; *Student Financial Aid; Tax Credits; Taxes; *Tuition
IDENTIFIERS	Paying for College; *Savings; *Tuition Prepayment

ABSTRACT

Summaries of conference presentations on college savings and prepayment plans and related tax, policy, and social issues are provided. The conference objective was to communicate the issues to constituents with the most at stake: parents, students, and relatives; state and federal legislators and staff; and developers of plans for higher education institutions and consortia. Panel discussions and speakers include: (1) "Welcoming Address" (Donald Stewart); (2) "Panel 1: College Savings Plans" (Michael O'Keefe, Theodore Bracken, Ross Hodel, and Lawrence O'Toole); (3) "Panel 2: College Prepayment Plans" (Aims McGuinness, Shari Caprara, William Moore, and Robert Bowman); (4) "Panel 3: Investment Issues" (Richard Anderson, Arthur Hauptman, Troy Murray, and John Finnerty); (5) "Keynote Address" (Frank Newman); (6) "Panel 4: Tax, Regulation, and Policy Issues" (Richard Anderson, Arthur Hauptman, Leo Raskind, Lawrence Owen, and Eric Toder); (7) "Panel 5: Issues of Risk to Providers and Consumers" (Arthur Hauptman, Richard Anderson, Herman "Dutch" Leonard, Lucie Lapovsky, Loren Hart, James Scannell, Janet Hansen, and David Longanecker); (8) "Closing Address" (Robert Atwell); and (9) "Closing Session: Summary Comments and Future Directions" (Haskell Rhett, Richard Anderson, and Arthur Hauptman). (KM)

****
* Reproductions supplied by EDRS are the best that can be made *
* from the original document. *
****

ED293395

INVITATIONAL CONFERENCE ON COLLEGE PREPAYMENT AND SAVINGS PLANS

SUMMARY

Denver, Colorado
July 7 and 8, 1987

Sponsored by:

American Council on Education
The College Board
Education Commission of the States
National Center for Postsecondary Governance and Finance

"PERMISSION TO REPRODUCE THIS MATERIAL IN MICROFICHE ONLY HAS BEEN GRANTED BY

CEEB

TO THE EDUCATIONAL RESOURCES INFORMATION CENTER (ERIC)."

U.S. DEPARTMENT OF EDUCATION
Office of Educational Research and Improvement
EDUCATIONAL RESOURCES INFORMATION CENTER (ERIC)

☐ This document has been reproduced as received from the person or organization originating it.

☐ Minor changes have been made to improve reproduction quality.

• Points of view or opinions stated in this document do not necessarily represent official OERI position or policy.

HE 021 147

COLLEGE ENTRANCE EXAMINATION BOARD, NEW YORK

A set of the conference summary and full proceedings may be ordered from College Board Publications, Box 886, New York, New York 10101-0886. The price is $10.

Copyright © 1988 by College Entrance Examination Board. All rights reserved. College Board and the acorn logo are registered trademarks of the College Entrance Examination Board.

Printed in the United States of America.

Contents

Preface ..... *v*

Speakers ..... *vi*

Welcoming Address *1*

Panel 1: College Savings Plans *2*

Panel 2: College Prepayment Plans *5*

Panel 3: Investment Issues *8*

Keynote Address *12*

Panel 4: Tax; Regulation, and Policy Issues *14*

Panel 5: Issues of Risk to Providers and Consumers *17*

Closing Address *22*

Closing Session: Summary Comments and Future Directions *23*

Preface

On July 7 and 8, 1987, four organizations joined together to sponsor the Invitational Conference on College Prepayment and Savings Plans described in this publication. It was my pleasure to welcome participants on behalf of the sponsors: the American Council on Education, the College Board, the Education Commission of the States, and the National Center for Postsecondary Governance and Finance. Now it is my pleasure to introduce this resulting publication.

Realizing that, across broad areas of higher education, financing plans and proposals are emerging faster than analysis, the sponsors joined in a common mission of organizing discussion and analysis among experts in the field. The objective was first to gain a better understanding of the issues and then communicate that understanding to the constituencies with the most at stake: parents, students, and relatives; state and federal legislators with their key staff members; and developers of plans for higher education institutions and consortia. It was our collective hope that this conference would assist in creating a positive climate for planning and developing nationwide college savings plans, informing legislative efforts at the state level during a critical time in the development of state-supported "futures" plans, evaluating current and planned programs in this area, and discussing and promoting the delivery of better information to families for college planning.

The dissemination of these discussions through this publication represents an initial step toward the realization of these objectives. All of us who helped organize the invitational conference are very grateful to the Lilly Endowment and the Teagle Foundation for their support of the conference and this publication.

Donald M. Stewart
President
The College Board

Speakers

Richard Anderson
Director
Forum on College Financing Alternatives
New York, New York

Robert Atwell
President
American Council on Education
Washington, D.C.

Robert A. Bowman
State Treasurer
State of Michigan
Lansing, Michigan

Theodore L. Bracken
Director of Federal Relations
Consortium on Financing Higher Education
Washington, D.C.

Shari Caprara
Legislative Director
Florida Student Association
Tallahassee, Florida

John Finnerty
Executive Vice President
CSB Holdings, Inc.
Princeton, New Jersey

Janet S. Hansen
Director for Policy Analysis
The College Board
Washington, D.C.

Loren Hart
Vice President Business/Finance & Treasurer
Swarthmore College
Swarthmore, Pennsylvania

Arthur Hauptman
Educational Consultant
American Council on Education
Washington, D.C.

Ross Hodel
Deputy Director
Illinois Board of Higher Education
Springfield, Illinois

Lucie Lapovsky
Director of Finance and Facilities
Maryland State Board of Higher Education
Annapolis, Maryland

Herman Leonard
George F. Baker, Jr.
Professor of Public Management
Harvard University
Cambridge, Massachusetts

David Longanecker
Executive Director
Minnesota Higher Education Coordinating Board
St. Paul, Minnesota

Aims McGuinness, Jr.
Assistant Executive Director for Higher Education
Education Commission of the States
Denver, Colorado

William J. Moore
President
Association of Independent California Colleges and Universities
Sacramento, California

Troy Murray
Cambridge Associates
Boston, Massachusetts

Frank Newman
President
Education Commission of the States
Denver, Colorado

Michael O'Keefe
President
Consortium for the Advancement of Private Higher Education
Washington, D.C.

Lawrence O'Toole
President
Nellie Mae
Braintree, Massachusetts

Lawrence Owen
Partner
Miller, Canfield, Paddock, and Stone
Lansing, Michigan

Leo Raskind
University of Minnesota Law School
Minneapolis, Minnesota

Haskell Rhett
Vice President, Student Assistance Services
The College Board
New York, New York

James Scannell
Vice President for Enrollments, Placement & Alumni Affairs
University of Rochester
Rochester, New York

Donald M. Stewart
President
The College Board
New York, New York

Eric Toder
Deputy Assistant Director, Tax Analysis Division
Congressional Budget Office
Washington, D.C.

Welcoming Address

Speaker
Donald Stewart, President, The College Board

Donald Stewart's welcoming speech set the agenda for the conference's discussion of college prepayment and savings plans. He reminded conference participants that whatever their views — and whatever the views of society outside the education community — of the causes, there is an imminent "affordability crisis" in higher education.

Mr. Stewart called for a national effort to assure that each family can pay its fair share of education costs, according to its ability. He urged the conference to work to assist in creating a positive climate for planning and developing nationwide savings plans for colleges; to guide state legislative efforts to develop future plans; to assist in evaluating current and projected programs; to promote better information for family higher education planning; and to identify means of fostering family investment and savings for higher education.

Although he did not endorse a specific strategy, Mr. Stewart defended educational payment planning as appropriate to supporting the educational futures of families at all income levels. As an educator with a long and active commitment to minorities, he portrayed such planning as vital for propagating the broad access to educational opportunity that has been a hallmark of American democracy.

Panel 1

College Savings Plans

Convener
Michael O'Keefe, Consortium for the Advancement of Private Higher Education

Panelists
Theodore Bracken, Consortium on Financing Higher Education
Ross Hodel, Illinois Board of Higher Education
Lawrence O'Toole, Nellie Mae

Presentations

Michael O'Keefe served as convener and discussant of the panel presentations. He began the session by suggesting that his experience of the past decade in the educational policy process confirmed Don Stewart's observations of rising educational costs and the need for reinvestment in education, making the notion of college savings plans a crucial one. In promoting the idea of such plans, Mr. O'Keefe suggested a dual purpose: to reawaken families to their responsibilities to save for higher education and to assist them in anticipating educational costs years in advance through effective and well-thought-out savings programs.

Theodore Bracken reviewed the conclusions on college savings of the Consortium on Financing Higher Education's study group on financing options and proposed an educational savings bond plan developed from the United States Savings Bond program. Mr. Bracken noted that the COFHE group identified several vital elements for a college savings program that could serve its needs, including attractiveness to all income groups; relative independence from federal subsidies; assured minimum returns, and returns keyed to inflation; broad utility of funds for educational purposes; and openness to contributions from all sources, not just parents and students. To meet such criteria, Mr. Bracken proposed an educational savings bond program. Such bonds, like U.S. Savings Bonds, would be guaranteed against loss and would be tax-free at state and local levels and tax-forgiven at the federal level if used for college expenses; would have a minimum rate of return keyed to the five-year Treasury-bill rate; and would be marketed through private sector involvement. Educational bonds would require special incentives and provisions, possibly including a federal tax-forgiveness provision when the bonds were used for educational purposes and exemption from the need analysis for grants and scholarships. Mr. Bracken also stressed the importance

of marketing in such a savings program and noted several traditional and innovative approaches that could be taken.

Ross Hodel sketched a state savings bond approach that is likely to go into effect in Illinois in late fall. After the Illinois Board of Higher Education studied educational savings and prepayment plans, a legislative task force appointed by the General Assembly recommended promoting savings, establishing incentives, and encouraging attendance at in-state schools. The state savings bond approach, one of four alternatives considered, would use much of the current administrative and financial structure for Illinois general obligation bonds. The new educational bonds would be issued as zero-coupon bonds yielding interest only at maturity instead of semiannually, and an interest bonus premium would apply if families proved that the funds were used for attending an in-state school. The investor assumes the risk that bond yields will keep pace with state higher education tuitions. The bills before the Illinois assembly also exempt educational savings from the need analysis for state scholarships.

Lawrence O'Toole discussed a savings plan that diverged from the notions presented by the other panelists. The primary focus of Nellie Mae is on an investment plan that relies on single-premium life insurance as the investment vehicle. Such a plan requires a sizable lump-sum investment and is intended to press families to invest for rising educational costs and to target their investment—whether to Ivy League tuitions, four-year public college tuitions, or other educational expenses. The investment's capacity to guarantee 100 percent of tuition would depend on the escalation of costs and the willingness of colleges to respond to the program; the program itself seeks to put families in "striking distance" of educational costs that, at a 7-percent per annum increase, could reach $32,000 by the year 2004. The plan is intended to give families the benefit of paid-up life insurance for the student and control of the funds, so that they may ensure that the funds are borrowed against exclusively for education. The plan would be administered by Nellie Mae, whose nonprofit status would dispel implications of Wall Street profit taking.

Discussion

To begin the discussion segment of the panel, Michael O'Keefe made several "framing" comments on the presentations before opening the subject to the audience. He suggested that the presentations had raised the issue of possibly competing or conflicting interests and objectives. For example, he noted the potential tensions between national and state or regional sponsorship of savings plans; between public and private sponsorship; and between the goals of merely shifting the existing savings patterns of families versus encouraging new savings. He suggested that if the underlying goal of savings plans was really to stimulate new savings specifically for education, the question of the type and adequacy of the incentives was vital. Here, he wondered how marketing costs or other "fine print" on bonds or single-

premium life insurance investments would cut into their effectiveness as college savings vehicles. The incentive issue also raised the question, he observed, of whether an outright tuition guarantee would prove necessary to encourage a long-term commitment to save for an expense that would rival or exceed the investment in owning a house.

On the subject of incentives, a member of the audience was intrigued by Ted Bracken's idea of involving employers in making contributions to educational savings bonds. He suggested that this practice could be fostered by seeking to build in a business tax break for corporations such as McDonald's for contributing to the college savings of its employees. Mr. Bracken responded that perhaps such corporations would find association with an educational bond program sufficient and would not demand such a tax break, and selling such a program might be more difficult politically because of the potential revenue impact. Ross Hodel, however, seemed somewhat more receptive to the idea of giving business an incentive, at least in comparing possible business contributions to education funds to current "401" plans in which employers are allowed deductions for matching workers' retirement savings. A representative of a retirement financing group cautioned, however, that such plans could be subject to nondiscrimination provisions that would vitiate their usefulness for educational purposes.

"IRA-type" savings plans also received some attention by panelists and audience. Mr. Hodel responded to a question on why Illinois did not seem to be pursuing an IRA-type approach, which would give a purchaser a tax deduction for the investment at the time of purchase. Illinois's present fiscal condition represents a roadblock to a state-based IRA-type bill, Mr. Hodel responded, although he noted that one had been drafted. Mr. Bracken also viewed the IRA-type approach with some doubt, suggesting that such a plan seemed more conducive to diverting savings—from retirement to education—than to stimulating new savings. Lawrence O'Toole agreed with the negative assessment, offering his experience as one of the authors of New York's PASS plan, a state-based IRA for education expenses that "has not been a booming success." The administrative costs were too high, Mr. O'Toole suggested, and the tax incentives too low, on a state level, to give families adequate incentive to invest. Ted Bracken summed up by suggesting that taking the foregoing weaknesses at the state level together with the IRA's troubles with Congress at the federal level made the IRA-type savings idea appear impractical in today's climate.

The question of savings incentives also surfaced in the group's discussion of their impact on the financial aid needs analysis process. A member of the audience raised the question of whether families would have the incentive to invest in a college savings plan under a system of needs analysis that would give them a larger financial aid award based on a lower current net worth. Yet, conversely, a questioner wondered whether exempting certain types of precollege savings would not also put pressure on the financial aid system by making it more likely that families with substantial savings or resources would become eligible for and interested in obtaining financial aid. Mr. Bracken responded by citing Michael McPherson's work urging adoption of a more adequate temporal perspective (over a child's eighteen years, say) for assessing family educational responsibilities in the need analysis process rather than limiting the focus to aid-based incentives and disincentives to

saving, which may play only a marginal role in the overall picture. In any case, Mr. Bracken favored a system that rewarded long-term saving by many over one that penalized a few for it.

Michael O'Keefe questioned some of Mr. Bracken's optimism about encouraging long-term savings, however, suggesting that it could be a serious problem to create an incentive for people to save at fifteen or seventeen years' distance from the possibility of realizing a benefit from the savings. Many people just may not have the faith that federal policy or tuition inflation rates would be predictable enough to bear out the wisdom of such investments. More relevant and effective, perhaps, would be the matching investment by a young person's employer—that would give the individual a rather immediate sense of the benefit the work and saving would bring.

The group also discussed the single-premium life insurance idea proposed by Mr. O'Toole. One member of the audience echoed Mr. O'Keefe's reservations about potential "fine print," mentioning administrative costs and penalties for withdrawal. Mr. O'Toole replied that he believed that the administrative and marketing costs would be relatively low because the work would be done from a nonprofit group's own office, bypassing commission sales, and would be supported by top-quality insurance firms that have the kind of history and investment expertise to make the notion workable. In response to a question about the participation of low-income families, he noted that they could use the policy itself as collateral to borrow the purchase price of the policy, though this would have tax and financial consequences in the event of forfeiture in the early years.

Panel 2

College Prepayment Plans

Convener
Aims McGuinness, Education Commission of the States

Panelists
Shari Caprara, Florida Student Association
William Moore, Association of Independent Colleges and Universities
Robert Bowman, State of Michigan

Presentations

Aims McGuinness, the panel convener, gave some brief introductory remarks and introduced the panelists. Mr. McGuinness acknowledged the national attention and popularity that the Michigan Education Trust (MET) had gained and said that a survey conducted by an Education Commission of the States (ECS) committee had concluded that probably ten or more states had passed or would soon pass similar legislation. But he cautioned that although many other states are considering Michigan-type legislation,

they are considering them within a wide variety of alternatives; for this and other reasons, the ultimate shape of prepayment plans is far from predetermined.

Shari Caprara spoke as a strong supporter of Florida's legislation, which closely resembles Michigan's. As legislative director for the Florida Student Association and as an undergraduate student, Ms. Caprara was closely involved in pressing for passage of the legislation and had a personal perspective on its impact. She argued that a plan that earmarked and safeguarded funds for educational purposes — as opposed to general family savings "intended" for children's education — was most protective of students. In addition, in contrast to complex annuity or insurance schemes, a relatively straightforward "Christmas club" educational savings plan was most likely to gain the trust and interest of families. Florida's plan, she noted, was intended to supplement inadequate state resources for student aid, to relieve the "middle-income squeeze" on families that do not qualify for adequate student financial assistance, and to involve families in a commitment to education that is reassuring to them and to the state.

William Moore voiced a number of criticisms of the Michigan-type plans. He argued that problems with the MET are symptomatic of the hasty and inadequate framing of many current prepayment arrangements. For example, Mr. Moore maintained that the ambiguous federal tax status of the MET could force the self-destruction of the plan as written. In addition, the MET-type financing mechanism requires highly optimistic returns on investment if the state or future participants are not to subsidize it inordinately. Mr. Moore also criticized the plan's lack of out-of-state portability, the fact that it would appear to force parents to make commitments for their children when the children were very young and not involved in the decision, and its implicit bias toward low-tuition public institutions. Mr. Moore argued that tuition plans should meet four basic criteria: (1) to supplement and not supplant existing student aid programs; (2) to enhance student choice; (3) to be nonpenalty portable; and (4) to be capable of relatively easy implementation. He suggested that rather than guarantee plans of the Michigan or Florida type, savings plans of a type being considered in Illinois or California may meet these criteria best. Such "ready-to-go, tax-exempt, state-sponsored college maximum-saver" programs would rely on bonds administered by a state tuition financing authority.

Robert Bowman vigorously defended the MET as one of its originators. He argued that the MET fulfills the four criteria that Mr. Moore raised, although he suggested that the intentions of the MET's framers were more broadly focused on making education available to those who ordinarily would not go to college rather than simply more affordable to those who would. He defended the MET in the contexts of relieving the social and economic crisis affecting minorities, meeting intensifying international economic competition, and responding to a broad public consensus in Michigan for an accessible, affordable, and secure educational system. He argued that the Michigan plan is workable with or without a favorable IRS ruling on its tax status and praised its flexible payment provisions, easy marketability, and range of

choice within Michigan. He maintained that the reality of a guaranteed tuition in place, even with "limits" on its portability, far outweighs a theoretical system that committees might discuss ad infinitum.

Discussion

The discussion centered on the Michigan and Florida plans. Responding to questions from members of the audience, Robert Bowman and Shari Caprara attempted to minimize the issue of possible federal taxation as an impediment to tuition prepayment plans. Mr. Bowman noted that a preliminary letter to the state of Michigan from the IRS seemed to indicate that the IRS's principal concern in granting a tax exemption to tuition prepayment plan participants might be whether participants' contributions to the MET were unambiguously structured as prepayment for educational services rather than as the participants' interest-bearing investment.

Although Mr. Bowman was confident that the Michigan plan would pass muster with the IRS, he acknowledged that in cases in which plan participants elected at term to attend a nonparticipating college, in or outside of Michigan, they would have to receive a cash return (equal to the average cost of tuition in Michigan), which then would be subject to federal taxation. Both Mr. Bowman and Ms. Caprara argued that any federal tax burden should not markedly impair the utility of the plans, however. First, the tax burden should fall on the student-participant and not on the parent-purchaser, so it should be relatively low. Second, the investment return could be paid out over four years, thus easing the tax burden.

A distinction raised in the discussion was between tuition guarantees and educational costs guarantees. Mr. Bowman said that Michigan would have liked to guarantee nontuition educational costs, such as room and board or books, but found it far too difficult to predict what the inflation rates of the relevant commodities would be, in contrast to predicting tuition rates, which tend to "smooth" over a period of twenty years or so. Ms. Caprara mentioned, however, that Florida might attempt to cover 70 percent of nontuition costs as part of its effort to market its in-state plan.

On the subject of a potential competition between prepayment plans and student aid, Mr. Bowman and Ms. Caprara both asserted that prepayment plans in their states would not divert funds that would otherwise go into aid programs.

Another subject was how effectively plan investment return rates could meet the tuition inflation. In cases in which the investment activity was contracted out to private firms, the fees paid to those firms might well cut into the profits, a member of the group supposed. In Florida, the state would regulate such fees, Ms. Caprara responded. The key issues, several participants agreed, were the degree of confidence with which states could project whether their investments would match tuition increases and the degree of cooperation future state legislatures would evince in subsidizing any shortfalls at the time guarantees came due. Mr. Bowman and Ms. Caprara were confident Michigan and Florida were prepared to meet shortfalls. But such subsidies might cut into the "fixed pie" of state educational resources, as-

serted one participant. Mr. Bowman countered by saying that in Michigan, educational requirements would be given an adequate share of an "expanding pie." William Moore protested, however, that expanding revenues and budgets were not characteristic for many states.

Panel 3

Investment Issues

Conveners
Richard Anderson, Forum on College Financing Alternatives
Arthur Hauptman, American Council on Education

Panelists
Troy Murray, Cambridge Associates
John Finnerty, CSB Holdings, Inc.

Presentations

Richard Anderson, co-convener, began the session by suggesting that the financial questions of prepayment plans are critical. He went on during the session to explain that there is more to them than tax advantage. Most important is the notion that a plan or a set of institutions can take a long-term investment perspective that is almost impossible for parents to achieve. Without a protracted investment horizon, parents tend to be constrained to investments with low yields — often these yields will be negative in real terms after taxes. Unless we can find an attractive investment vehicle for parents saving for college, he asserted, they will continue to use the home as their primary way of accumulating capital.

Arthur Hauptman was added to the program as co-convener to provide some background on recent tuition increases as a context for the discussion on investment income. He noted that a recent American Council on Education study he helped conduct came up with four relevant findings: (1) that tuitions are rising rapidly in the 1980s; (2) that recent tuition increases have not been limited to selective private schools but have affected most institutions; (3) that the tuition increases of the 1980s have outpaced inflation, whereas those of the 1970s lagged behind it; and (4) that the relation between measures such as growth of disposable personal income or median family income and tuition increases is not straightforward or a very reliable predictor. Mr. Hauptman argued, in the context of predicting future changes, that tuition increases may outpace inflation when it is low or lag behind it when it is high; they appear to vary within a narrower range than inflation of perhaps 5 to 11 percent, depending on inflationary considerations.

Troy Murray suggested that to be financially self-sustaining, a college savings or tuition guarantee plan must achieve a return on its investments at least

equal to the institutional inflation rate plus the plan's management costs. This implies a 3- to 4.5-percent real (inflation-adjusted) return per year. Although the average annual real return on common stocks has exceeded 6 percent, the year-to-year volatility in common stock and even bond returns complicates the investment task. When tuition must be paid only a few years from now, preserving capital will be more important than earning a real return. When this tuition "liability" is ten or fifteen years away, however, a real return may be sought from somewhat riskier equity investments. A risk with any plan is that market volatility or poor management may require later joiners to pay a disproportionate share of the costs. Even under optimal conditions, parents may be forgoing potential investment returns in order to participate in a college savings or prepaid tuition plan. Mr. Murray argued that these plans should be held to securities law disclosure requirements regarding risks and assumed rates of return. He emphasized that such programs should have a reserve against market variations. He posited that a nonprofit, national "Common Fund for Parents" might provide the safest, most flexible, and most portable mix of savings choices.

John Finnerty also noted the volatility of investment returns. He focused on the questions of the necessary rates of return a plan might expect over the life of a tuition future and how the sponsor should price the plans in the light of volatile returns. The financial integrity of a tuition payment plan, he told the group, will depend on its pricing, its rate of return on investment, and its degree of cross-subsidization (i.e., the number who invest but ultimately withdraw, sacrificing interest and dividends to the system, over the number who actually use the benefits). On these measures, Mr. Finnerty looked at the plans at Duquesne University and in the state of Michigan. At its current prices, escalated at 7-percent inflation per year for fourteen years, the Duquesne plan would require a cross-subsidization of 2.66, implying a rejection or withdrawal rate of about 73 percent, assuming no premium in the rate of return on investments above inflation. At the other end of the spectrum, with a 7.21-percent premium in the rate of return on the investment above the college inflation rate (i.e., a 14.21-percent rate of return each year for fourteen years), the required cross-subsidization would be zero. The Michigan plan, over the same fourteen-year period, would require a cross-subsidization of 1.0 at a zero premium or a 3.49-percent rate of return premium above the same projected 7-percent inflation if there is no cross-subsidization. At Michigan's prices, at only a 2.5-percent rate of return premium, the required cross-subsidization would be 0.20, or a relatively realistic one withdrawal for every five participants. Mr. Finnerty concluded that given realistic expectations of returns and cross-subsidization, the Michigan plan is aggressively priced, probably somewhat underpriced, whereas the Duquesne plan appears to be severely underpriced.

Discussion

The discussion of the panel on investment issues focused largely on the merits and potential problems of tuition prepayment plans. Although ac-

knowledging that there would be problems in getting a workable plan that was fair to both investors and institutions, Richard Anderson defended prepayment plans as capable of offering significant advantages compared to investment by individuals. The size and continuity of plans would allow them to follow sophisticated investment strategies and perhaps even to mitigate the effects of cyclical market variations that would jeopardize the funds of individual, short-term investors. Moreover, Mr. Anderson said, financial planners might be able to tailor investment goals to the specific inflationary considerations affecting college tuitions (e.g., labor-cost inflation). Potential tax advantages could also be a factor, he said. Even the Duquesne plan, admittedly highly risky for the university, may have had the goal of attracting and motivating new attendees who would not have saved otherwise.

Other panel members and members of the audience questioned whether prepayment plans had a unique capability to provide advantages and wondered whom such plans would benefit and whom they would expose to risk. One participant calculated that a risk to participants in a state plan was that if the student chose to cash out of the plan to attend a nonparticipating or out-of-state school, the additional tax burden could turn out to be perhaps $3,000 on a gross return of $13,000. Mr. Murray allowed that plans might be beneficial in some cases, especially to those who were committed to an in-state, participating school and who sought a Christmas-club-type savings discipline, but that other types of investments, such as a national Common Fund, might be less risky to individuals and issuing institutions.

The discussion appeared to suggest that a key issue in judging a plan's utility, focus, and risk would be the degree of the discount offered to plan purchasers. The group agreed that extreme discounts, apparently the strategy at Duquesne, would certainly attract investors. The university here appears to be taking the high risk that it could build those investments and utilize cross-subsidization earnings to keep the plan solvent. Michigan's plan discount vis-à-vis current tuition is about a third, one participant noted.

The panelists then wondered who would use such plans. If the discount were decreased, less-well-off citizens might not be able to afford them, whereas if it were maintained, the states and universities might have to absorb significant plan losses, which in most states with limited education budgets could injure student aid to lower-income groups. Mr. Murray, Mr. Hauptman, Mr. Finnerty, and Mr. Anderson appeared to agree that deep discounting or underpricing of plans—no matter how attractive it made the plans to potential investors—was likely to cripple them financially in the long run. Discounts, Mr. Anderson proposed, might come later, after plan investment performance and delivery were established.

At least one participant defended the discounting, noting that Florida and Michigan justified it not only because it assists in marketing the plans but because they felt able to satisfy the financial requirements of the plans through investment performance or subsidization and because they expected to limit participation in the plans to cap the risk. A group member expressed skepticism about the equity of "exclusive" plans and asked whether lower- or even middle-income groups would be able to put down considerable lump-sum investments that plans could require. But plan proponents responded that tuition prepayments were not really designed for the lowest income groups, which would rely on student financial aid.

The panel did not come to a firm judgment on the implications of an important consideration, again relating to the equity issue, raised by Mr. Hauptman: Would typical financial aid grants to low-income students — ranging in Michigan, for example, from $1,400 to $2,400 — represent a smaller subsidy in absolute dollars than the discounts subsidized plans would yield to middle- or upper-income groups?

Mr. Finnerty concluded by noting that the tendency of plans to discount made the character of the plan-issuing institution an important factor in the viability of the investment. States that could raise taxes or reallocate funds to cover shortfalls would be far better placed to guarantee tuitions than would a small college with a limited endowment. Richard Anderson agreed; he added that single-institution plans also carried the risk of loss of educational integrity; that is, if the institution dropped programs or lost accreditation, the risks would be unfairly shunted onto plan investors.

Keynote Address

Speaker
Frank Newman, President, Education Commission of the States

Frank Newman, after an introduction by Don Stewart, spoke to the conference on the values underlying the fundamental social question of access to education. Mr. Newman sought to shift the participants' focus from the technical details of various programs to the critical value choices that educators must bring to consciousness as the basis for effective planning.

He suggested that in the present epoch of historic development, our civilization has more than adequate resources, if we choose to bring them to bear, to underwrite a broad-based, nonelitist education, in keeping with the traditional egalitarian goals of American society and the present social consensus.

He raised eight basic value questions about which critical social policy choices must be made and suggested a few answers: (1) Do we believe in subsidizing education for the less-well-off? Here, Mr. Newman suggested that Americans probably believe neither in taking everything from the rich nor in leaving the poor to their own devices but rather in a modified but effective subsidization of the poor. (2) Should this generation subsidize the next? This issue is complicated by the extended educations and returns to education now becoming commonplace, which make financial obligations overlap the generations. (3) Can colleges remain or become pathways for general social mobility? Employment trends suggest, and the consensus of American opinion supports, the idea that education should be an avenue of mobility. (4) Do we believe that all students ought to start life after graduation without the financial burdens of excessive loan repayments? Mr. Newman answered yes, emphatically, because such obligations put a disproportionately heavy burden on the aspirations of the less-well-off. (5) In a related question, he asked whether we believe students should be able to pursue careers based on their authentic aspirations rather than ones based on "the kind of financing that is available." Again, Mr. Newman spoke forcefully for a more genuine self-determination as appropriately expressive of the deep-felt beliefs of Americans. (6) Similarly, he argued, college choice should reflect the genuine preferences and abilities of students and their families and not choices based on a multiple-level, elite tracking system of the type found in some European countries. (7) Do we have the right incentives for students, families, and institutions? Mr. Newman argued for the value of student employment as a means of financing education, but at rates of pay, even subsidized pay, that would make student employment a financially meaningful contri-

bution. (8) Must we, and can we, address the issue of rising college costs? Mr. Newman argued that "greed" is not a major factor in rising costs and that most increases are justified, but that cost containment should be discussed.

He concluded with four proposals: (1) Think in advance on these issues. (2) Clarify the underlying values, such as work, social commitment (as opposed to the yuppie "ethic" of work exclusively for self-gratification), egalitarianism, and family support and responsibility. (3) Involve the public in shaping and refining a consensus for educational policy; a nonelitist policy cannot be built exclusively by technicians. (4) Recognize the need for change, for, in the words of the hymn, "Time makes ancient good uncouth."

Panel 4

Tax, Regulation, and Policy Issues

Conveners
Richard Anderson, Forum on College Financing Alternatives
Arthur Hauptman, American Council on Education

Panelists
Leo Raskind, University of Minnesota
Lawrence Owen, Miller, Canfield, Paddock & Stone
Eric Toder, Congressional Budget Office

Presentations

Richard Anderson introduced the panel and sketched some of the important tax questions. These include the following: Will there be an income tax? A gift tax? If there is a tax, to whom will it apply? When will it apply? How stable is an Internal Revenue Service letter ruling likely to be?

Leo Raskind began the presentations by setting out the relevant tax issues of prepayment and savings plans. He noted the economic importance of tax treatment, because such plans are designed to accumulate funds, so that the central concern is the net available for tuition after taxes. Uncertainty about the tax treatment of the several transactions involved in such plans serves only to cloud and inhibit the acceptance of the plans.

Taking the existing and proposed plans together, two federal taxes are involved—the federal gift tax and federal income tax. The initial transfer of prepayment to a fund or trust for the future benefit of a student raises the issue of whether this is a transfer of value subject to the gift tax. Under general tax principles, it would appear to be taxable unless the transfer were characterized as essentially a transfer to an educational institution and thus exempt. The same transfer may also generate potential income tax liability in a variety of ways. The initial transfer to the trust for the future benefit of a student might be viewed as income to the student when it is disbursed for his or her benefit. During the period when the funds are held and invested by the trust, the interest or dividends on these invested amounts might subject the trust to income tax liability. If there was a refund that included some interest, there could be income tax liability to the refund recipient. The significance of income tax considerations is underscored by the fact that the Michigan statute will not become operative until the pending request for a favorable ruling from the IRS is received.

Mr. Raskind characterized original issue discount and time value of money considerations as potential tax complications worthy of further discussion.

Lawrence Owen discussed the tax issues as they apply specifically to the Michigan Education Trust (MET), whose interests his firm has been defending before the IRS. He argued that participants in the MET should not incur a gift tax because parents are simply purchasing educational services, not realizing a money profit. The trust itself should not be subject to federal taxation because the state legislation is carefully structured to bring the MET under the umbrella of intergovernmental tax immunity. The personal taxation issues are more complex, but the narrowly drawn refund provisions should protect the investor from taxation under the notion of constructive receipt during the term of the contract. The substantive issue is whether the IRS will rule that there is tax due on the appreciated value of tuition at the time the student collects on the original investment. Mr. Owen cited a variety of precedents to the effect that it should not be taxed. For example, he noted that people who make extensive use of services or a contract for which a fixed fee has been paid — say, a Health Maintenance Organization or an appliance maintenance contract — are not taxed on the increased value of the services they receive, nor are they able to claim a loss if they do not use the services. Only if individuals take a cash refund should they be subject to tax, and here the tax should fall on the student, who is usually in a lower income bracket. Mr. Owen suggested, as well, that the time value of money issue should not be considered relevant because of the absence of a specific debt instrument. He expressed the hope that the IRS would rule positively and the belief that the MET represents a "major breakthrough" in higher education financing.

Eric Toder discussed the tax questions from the perspective of public tax policy. One danger in exempting a class of investments from taxation is that those investments may be used for tax avoidance rather than for the principal policy purposes intended. This was the case with Individual Retirement Accounts (IRAs), he noted, when banks profited by loaning individuals money to invest in IRAs, at the same time allowing the individuals to accumulate interest tax-free and deduct borrowing costs.

On the subject of original issue discounts and the time value of money, Mr. Toder suggested that educational savings or prepayment plans may fall under the rubric of disguised loans, in which, despite an apparent absence of interest being paid, there is an implied interest rate. In an economic sense, this interest accrues to the parent but is sheltered by the tax-free status of the university. He suggested that such devices were analogous to industrial development bonds (IDBs), through which states extended their tax immunity to corporations borrowing for specific private development projects considered desirable. But he noted that the federal government tolerated IDBs only until their use became widespread. And he added that given the potential impact of widespread educational savings or tuition guarantee plans as tax expenditures, the government might well respond similarly, especially if the plans appear to be sheltering the income of those in the upper tax brackets.

Mr. Toder disagreed with Mr. Owen's interpretation of the locus of tax

liability at term, suggesting that if the parent pays for a tuition guarantee, the return should not be attributable to the child, just as when a parent pays for a child's education while the child is in college, this is not considered the income of the student but of the parent or of whoever made the investment. To avoid the disadvantage of taxation on realization, the government designed an education savings bill, now defunct, in which the low-to-middle-income groups could deposit money that would be taxed initially but would accumulate and could be withdrawn for legitimate educational purposes tax-free. Mr. Toder expressed some skepticism about the political viability of plans that would allow deductions on deposit and no taxation on withdrawal because their rates would exceed pretax rates of return. He also questioned the public policy efficacy of tax incentives targeted narrowly at specific groups because they would not enhance overall savings. Consumption-based taxes, rather than income taxes, would alleviate the disincentives to savings at a social level more effectively.

Discussion

The discussion delved into some of the details of the tax questions raised by the three panelists. Of particular interest to group members was the pending IRS ruling on the tax status of the Michigan Education Trust (MET). In response to a question on the contents of the eight-page IRS letter, Lawrence Owen noted that the letter was not public to his knowledge and did not offer a definitive statement, which will come only when the statute has been put into effect. The immediate IRS concerns, Mr. Owen related, regarded the time value of money and the nature of the relations between the trust, beneficiary, state, and institutions of higher education. As in his presentation, Mr. Owen stressed that the "bedrock notion" of the MET was that participants were paying for a service that, though it might appreciate in value, should not be considered an investment yielding income to the purchaser. The four years of education being paid for, he said, should be considered in the same category as any service consumed by the purchaser. John Collins, Mr. Owen's partner, agreed, making the analogy to a commodity such as a bushel of corn: "If you buy an asset that appreciates in value between the time you buy it and when you use it...you normally do not have income."

Certain potential complications in any IRS ruling were noted by panelists and group members. Leo Raskind mentioned, in response to a question, that even if the IRS ruled completely in favor of the MET, it could reverse itself if in practice the program contravened its intended or stated goals — for example, if the plan was turned into a large tax shelter and surreptitious marketing became prevalent. Another participant asked whether the IRS had raised the question of the price discount of many plans as susceptible to taxation. Messrs. Toder and Raskind replied that the IRS had not raised that question directly, but that it was implicit in the IRS's concerns about the structure of investor-plan relationships and could become an issue. Michigan, however, has a constitutional structure that would probably allow it to justify discount marketing of the plans as an aspect of its effort to secure the general welfare and education of its citizenry, Mr. Raskind noted.

Another subject of some interest was the tax status of funds taken out of a plan for use at nonparticipating or out-of-state institutions. Mr. Owen agreed with a questioner who asserted that income "cashed out" of the MET would be much more difficult to defend from taxation. Yet Mr. Raskind suggested that perhaps some steps might be made to protect the money from taxation, and a group member speculated that making the payments directly to the colleges, rather than to the student or parent, might protect the funds somewhat. Finally, a participant suggested that the higher lifetime earnings, and therefore tax payments, of college graduates might at least be taken as a good social or economic reason to exempt program cash-outs from taxation if the funds were used for higher education.

Exactly how prepayment funds, or student aid, or scholarships would be taxed appears to be an issue of broad significance. Tax reform legislation, one member of the group noted, is tending toward taxation of scholarships, and the question of the equity of taxation on other forms of educational financing becomes relevant. Mr. Raskind noted, however, that the recent tax code revisions (Section 117) may be aiming more at stopping abuses of certain types of financing, such as of government grants aimed at encouraging people to go into teaching that are being misused by institutions or by people who have no real intent of following through.

Panel 5

Issues of Risk to Providers and Consumers

Conveners
Arthur Hauptman, American Council on Education
Richard Anderson, Forum on College Financing Alternatives

Panelists
Herman "Dutch" Leonard, Harvard University
Lucie Lapovsky, Maryland State Board for Higher Education
Loren Hart, Swarthmore College
James Scannell, University of Rochester
Janet Hansen, The College Board
David Longanecker, Minnesota Higher Education Coordinating Board

Presentations

Arthur Hauptman introduced the six-member panel and made a few remarks to set the context for the discussion of issues of risk to providers and consumers. He noted that tuition guarantees and savings plans each have risks. He singled out the educational risks to students if they would rather not go to one of the institutions covered by a plan, or the risks to institutions, which might come under pressure to make admissions decisions based on

candidates' participation in a plan. He also cited the financial risks, especially that tuitions would increase faster than the earnings of plans. Such risks never disappear, he warned, but are shifted among the three typical participants in a plan: the states, the institutions, and the consumers.

Dutch Leonard began the discussion of risks to the states. He suggested that the core of the present problem in financing higher education was the inadequacy of middle-income savings. An important reason for the savings shortfall, he noted, is the difficulty of securing an adequate return on savings after taxes and inflation. But perhaps equally important, he suggested, is the lack of a convenient and trustworthy mechanism for educational savings. Tuition prepayment plans might be an answer to these problems, if, out of a commitment to furthering education, the state and the colleges were willing to take the initiative and risk to overcome these barriers. The question then would be to assess how great the risks are.

Mr. Leonard outlined a plan that is being designed in Massachusetts to serve both private and state schools. He focused on the plan's "certificated tuition prepayment" component, which would allow consumers to buy certificates entitling them to specific amounts of tuition at different Massachusetts schools. A $1,000 certificate, for example, might buy 10 percent of a year at a high-tuition private college or 50 percent of a year at a lower-tuition state school. The certificates are thus relatively portable. Colleges take the risks that tuitions will not outrun the investment returns of the plan, but the state takes a risk in guaranteeing a floor return.

He noted that preliminary "worst case" simulation modeling based on historical data has suggested that the plan's potential losses would be minimal and its potential gains significant. Full-scale risk analysis is under way. He concluded that the plan's principal benefits are that it is attractive to parents, students, and others who want to contribute to education; that the certificates have potential portability to regional and possibly national scale, especially if different states could coordinate their guarantees; and that the returns are potentially great compared to the risks. Although still incomplete, the plan offers great promise, Mr. Leonard said, and he welcomed comments and input on its development.

Lucie Lapovsky continued the discussion of state risk. She raised the question of whether locking itself into a commitment to guarantee tuitions at one level would prevent a state from changing its overall tuition and financial aid policies later on. In addition, she suggested that if a subsidy were required as a marketing incentive for tuition certificates or savings plans in states with limited education budgets it could end up being taken out of other parts of the education budget and at the least would act as a tax for the benefit of middle-income savers. In addition, a risk of such a program is that it might prove a politically convenient way for legislators to subvert traditional financial aid programs or to discriminate against students whose families have failed to save or participate. If plans can be designed to be attractive without subsidies, she said, this might relieve the state of some of the burden and risk and might protect other aspects of the educational financing system.

Loren Hart started off the discussion of risks to public and private institutions. Private university and consortium plans, Mr. Hart noted, are essentially

moribund because of the unsettled tax situation, the public relations risks in offering institution-specific tuition guarantees and then having to deny admission to some purchasers, and the development risk of confusing purchases with donations.

Thus, the principal question is the risk to public and private institutions from state-based plans. For the public institutions, one risk is that investment losses in a plan will then be reimbursed by cuts from the state's higher education fund. A second risk is the losses that low-tuition public universities might sustain if locked into low-rate guarantees in a time of sharply rising costs. A third risk, in a plan that offers a uniform price that might cover institutions of widely differing quality and attractiveness, is intensive demands for admission to the top schools. Also, how would such plans affect schools that were trying to restrict their admissions?

For private universities, the principal risk is in the implicit advantages given to public universities, largely due to the limited portability of plans. Mr. Hart suggested that the existence of a private educational system relieved the tax burden on the public system and questioned whether the proliferation of nonportable state-based plans did not traduce the principles of a national educational system.

James Scannell also spoke on risk to public and private institutions and boosted the dual, public-private, system. Tuition guarantees would not appear to be a common ground between the two sectors because of their widely differing financial bases. Rather, a plan or "cafeteria" of plans that enabled families to save to their capacity would be ideal. Portability and maximum leverage for the funds are the prime criteria; on the latter point, the possibility of soliciting contributions from employers or to the fund for community service work might be effective means.

Janet Hansen began the discussion of risk to consumers. She noted that the likely situation in the near future was proliferation of plans by entities of many sorts — states, nonprofits, profit-making groups, consortia, and so on. Probably it is good to "let a thousand flowers bloom," she acknowledged, but meantime, the multiplicity may make choices by consumers difficult and risky.

Dangers lurk for students even before the plans are in effect, because the plans may impinge on student financial aid programs and may deflect attention from deserving constituencies or programs. Similarly, once the plans are in full swing, nonparticipants may face discrimination. Also, the question arises of whether the plans are adequately flexible to meet the needs of the very large proportion of students who don't go to college immediately, who don't finish, or who drop out and return. This is a crucial issue for minority groups. The issue of whether an effective plan needs to cover the entirety of educational costs should be raised, Ms. Hansen noted. Another question is whether high rates of geographic mobility could expose many original purchasers now living out-of-state to nonresident tuition rates — or if they didn't, would this be a form of discrimination against other out-of-state students?

Finally, there are semantic dangers: *guarantee* and *educational services* may mean different things in different plans, so that the only effective protection for consumers may be in developing a full-disclosure rule or system.

David Longanecker was the final panelist. He shared six criteria that the Minnesota Higher Education Coordinating Board has been thinking about as possible guidelines for consumers. First, eligibility criteria: In the light of interstate mobility, is it wise to purchase a Minnesota plan for a two-year-old if one may be transferred to Texas? In the same vein, what age restrictions might apply? What about income requirements for participation at the top or bottom ends of public or private plans? Second, the breadth of opportunities a plan actually provides: For example, a plan may be severely limited by the fact that very few institutions are participating fully in it. Third, how costs are covered: Will such plans cover only tuition and fees? Or all legitimate educational expenses? In a similar vein is the question of the application of penalties or sacrifice of benefit: Would a student who left school after two years be able to recapture the value of a four-year tuition investment later? To do so would be consistent with the concept of life-long learning, but appears not to be typical of the financial structures of most plans. Fourth, the flexibility of financing: Does it allow for adequate savings? Mr. Longanecker argued that it would be unfortunate to have to have separate programs to cover different aspects of what is a single experience or commitment. Fifth, the qualifiers in the plan: Do they protect the consumer in the case of a death, dropout, return, and so on?

Sixth and last, Mr. Longanecker stressed the quality of the investment: Will its benefits outweigh the likely risks? He noted that he favored savings plans, because they offered the possibility not merely of keeping up with risks but of actually outrunning them. Moreover, he pointed out, savings plans give a much more positive social message: Rather than representing an insurance against catastrophic rises in tuitions — a negative idea implicit in the marketing of guarantee plans — savings plans imply the positive values of foresight and ability to reap the benefits of delayed consumption.

Discussion

Much of the controversy in the discussion segment of the fifth panel revolved around the Massachusetts plan outlined by Dutch Leonard and around the concept of "winners" and "losers" in various types of plan arrangements. To begin the discussion of risk, Arthur Hauptman raised the question of just how much risk there was. His point was that this might determine just how necessary and valuable savings and prepayment plans would be.

Mr. Leonard responded by suggesting that plans implied some degree of risk, because to keep up with the rate of inflation, investments would have to be of a fairly risky sort. Like other proponents of tuition guarantees, Mr. Leonard asserted that the value of prepayment and savings plans was precisely in their ability to pool investment risks among institutions and across time, so that the plans' participation in relatively risky forms of investment could yield a higher long-term rate of return than an individual parent-investor could safely attempt.

Mr. Hauptman was not convinced, however, that plans could be devised in which "everybody wins." He speculated that Mr. Leonard's view implied that states would actually be spreading the better returns on one investment

cohort's money to cover the lesser returns on another's, thus victimizing some consumers for the benefit of others. Mr. Leonard disagreed with that viewpoint. What should matter to participants, he argued, is not the precise return on their particular monies but the long-term stability of the fund in guaranteeing the service of education to prospective students.

David Longanecker suggested that the guarantee, "peace of mind," and "ability to sleep at night" aspects of the tuition prepayment plans amounted to a form of insurance, and that as such, plans might well be judged by individuals against insurance plans or other forms of investment intended to perform well vis-à-vis inflation. Another concern, voiced by Janet Hansen, was over the initial discounts offered by plans: Would these not handicap the plans' abilities to keep pace with inflation? Against these reservations, one member of the audience suggested that an underrecognized value of savings plans specifically geared to education was their psychological impact in motivating families and students to perceive education as financially accessible to them. A possible solution to mediating between the attractions and dangers of investment in a plan for consumers was offered by a member of the audience who had participated in designing the New Jersey plan. He noted that in its current form in the state senate, the plan attempts to include the consumer, colleges, and beneficiaries in gains beyond the 90-percent level.

As the Michigan plan had attracted considerable attention in previous sessions, so the Massachusetts plan outlined by Mr. Leonard now came under closer scrutiny. Proponents of the Massachusetts-type guarantee plan suggested that its public-private balance, wide applicability, regional character, and invitation for participation by other out-of-state schools made it a possible template for an eventual broad-scale, workable higher education financing device. At worst — in case the student attended a nonparticipating out-of-state school — the plan would return cash in the appreciated value of the fund; thus, prepayment plan proponents argued, its fall-back would be to become essentially the savings plan that critics of prepayments were supporting.

Critics suggested that this picture had flaws. One participant noted that a plan designed as a Massachusetts tuition guarantee might not represent the best savings plan available for students out-of-state. In addition, he recalled the unresolved tax issue as a danger to the out-of-state portability of Massachusetts-plan monies. Another group member wondered whether out-of-state residents whose local university was participating in the Massachusetts plan would be permitted to enjoy Massachusetts' state guarantee of their tuition and what problems that would create with state legislatures.

The session ended with a reprise of the discussion of Mr. Hauptman's initial questions about the degree and locus of risk: Did the investment diversification offered by tuition guarantee plans amount to a "zero-sum game" in which some investors had to "lose" in order for others to "win," as Mr. Hauptman had suggested? Mr. Leonard reiterated the contention that net gains could result from transferring risk to those more willing to bear it. In addition, another member of the group argued that diversification over time could yield a net economic gain because the total cost of risk bearing would be reduced, not just transferred. It would be a positive-sum game then, he noted, but he added that fair pricing would be essential to making "everybody win."

Closing Address

Speaker
Robert Atwell, President, American Council on Education

Robert Atwell addressed the final luncheon meeting of the conference. Mr. Atwell said that he believed that tuition guarantee programs were in general a bad idea, but that in part, the higher education community had brought financial troubles on itself by allowing itself to become captive to the non-educational "lending community" and by neglecting the needs of middle-income families who are now clamoring for guarantee programs.

The prime point, Mr. Atwell said, was to view college savings and prepayment plans in the context of who is and who ought to be paying for college. The current situation is not good. The increasing loan burdens that are created by rising tuitions and declining student aid mean that financial responsibilities now are increasingly falling on the students themselves. Federal and state government efforts are of declining usefulness. The Guaranteed Student Loan program exacts a high cost from the government. The Pell grant program, targeted toward low-income students, is expensive and not very cost-efficient and has not been keeping up with student need.

Therefore, a new vehicle for assisting students, one that will assist middle-income students as well, is needed. Such a program would not require a direct subsidy to students but instead could use a federal guarantee or insurance to help middle-income students spread the financial burden of attending a pricier institution over a considerably longer period. Savings plans or tuition guarantees, to work effectively, would have to be national and not institution- or state-based plans, he concluded.

Closing Session

Summary Comments and Future Directions

Convener
Haskell Rhett, The College Board

Panelists
Richard Anderson, Forum on College Financing Alternatives
Arthur Hauptman, American Council on Education

Presentations

Haskell Rhett began the summing-up session with some observations on the conference's objectives and its "unfinished agenda." He noted that the conference had aimed at creating a climate for development of a nationwide savings plan, at informing legislatures that are developing savings and futures plans, at evaluating current plans, at discussing how to provide better consumer education planning, and at discovering how to foster family educational savings. Progress to date on this long-term agenda might be summed up as follows: The conference reached no consensus on the shape of a national plan but seemed to express strong interest in continuing attempts to discuss and develop one. The exact nature of an approach to providing consumer information also seems to be open, but again, broad support seems evident for developing guidelines, and the sponsors will continue work on that. The conference raised intriguing questions about the need for analytical models and value structures to assess plan impacts, risks, and requirements (for example, subsidies, incentives, or marketing techniques).

Richard Anderson suggested that both sides — those for and those against prepayment plans — have valid points. A serious drawback to prepayment plans is that legislators may be tempted to promise too much, to sell future tuition at a discount with too little concern for the long-term financial stability of higher education. He also observed that prepayment plans can be used to restrict choice. This problem, he went on to say, is not restricted to the prepayment notion, however. Legislators in at least one state have designed a *savings plan* for parents that will tend to limit out-of-state attendance.

The real value of the prepayment concept is in the potential ability of institutions to take a long-term investment perspective, Mr. Anderson maintained. Families saving for higher education are not able to take a protracted

view because they need the money in a set period of time, and this need greatly reduces their ability to place funds in high-yield investments. Mr. Anderson concluded by observing that the commercial sector is now creating its own plans; the fundamental goal of these plans is to produce profit, however. A national set of colleges and universities could create a better plan, he argued, and one that would retain greater financial advantages within higher education.

Arthur Hauptman responded to Robert Bowman's assertion that opponents of the Michigan tuition guarantee appeared afraid to take a stand. Mr. Hauptman said that as a critic of the Michigan plan he was not at all unwilling to take a stand: Guarantees may be beneficial in some cases, but they are inordinately risky to consumers and institutions because of their circumscribed portability. He argued that education plans should not rely on transferring risk to other participants or to students who do not participate. Mr. Hauptman favored savings plans because of their broader applicability and portability. He stressed that planners should consider ways to minimize the chief consumer risk by seeking to ensure that plan investments and tuitions remain within reach of each other.

Discussion

The closing session discussion was more freewheeling than the individual panel discussions, as participants ranged over a variety of themes and considered the prospects and directions of prepayment and savings plans.

Several proponents of prepayment plans urged the group to recall the need for relatively high-risk investments, guaranteed by a plan or institution, as a key to encouraging parental savings for education. The prime issue, one participant suggested, was that parents had to have a reasonable expectation that following what would be for them a long-term savings discipline would allow them to keep up with tuition inflation. They cannot assure this individually, plan proponents stressed. The purpose of plans, then, should be to protect individual families from the dual risks of putting their funds into safe but subinflationary-yield instruments or of putting them into aggressively managed funds that promise high yields but may be in a down position when families need the cash.

Dangers of rhetoric and facile judgment were highlighted by some of the discussants. One noted that the "Christmas club" rubric for savings and prepayment plans, though familiar to many families, should be discarded because of its connotation as a low-interest vehicle. Another participant pointed out that many "statistics" being cited as the basis for evaluating plans such as Michigan's are still preliminary and should not be made the basis of irrevocable judgments.

On the issue of equity (originally raised by Art Hauptman) one member of the group suggested that the public policy goal of plans should not be to equalize subsidies (e.g., in the form of discounts or tax advantages) for savings or prepayment plans with those given in the form of financial aid. This view appeared to speak to the tendency in the conference to see plans' primary

goal as encouraging the maximum amount of family saving for education. This perspective was reinforced by those who argued that a principal task of new plans was changing or expanding family saving behavior through providing comprehensible instruments, publicity, and adequate incentives.

Another point raised was the possibility of guaranteed yield versus guaranteed tuition. If savings plans could yield 3 percent above inflation, one participant suggested, this should be adequate to cover tuition inflation, and if it is not, the difference may be beyond the scope of a plan's responsibility — for example, if improvements or changes in service were a cause for higher charges.

Some participants hoped that some kind of national guarantee agency would be able to provide criteria of nonprofit status, guarantees, portability, and adequate returns. Several attendees responded to the issue of portability and endorsed a national savings plan or Common Fund administered by a nonprofit organization and bearing a tax exemption as an incentive. Others were skeptical that such an agency could or would engage in sufficiently dynamic investments to make the program workable. One participant who was skeptical about a rapid push for a national strategy expressed doubt that such a plan could speak to the highly differential needs of the various states. The states, in this latter view, can serve as laboratories for solutions — such as how to treat plan earnings in relation to inflation, what are proper levels of discounts and efforts at marketing, and so on.

An apparent consensus of the group, however, was that despite the criticisms voiced of virtually every strategy, action — even if imperfect — may represent a substantial improvement over the status quo. Moreover, whatever the particular strategies favored by individual participants, all appeared to agree that, in the spirit of "a thousand flowers blooming," interest in and pursuit of national and state plans would continue to develop.